

ADJUSTMENT VIA AUSTERITY:

IS THERE AN ALTERNATIVE?

Norman P. Girvan

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Girvan, a former director of national planning in Jamaica, under Michael Manley, was a key participant in the South-North conference on the international monetary system and the new international order in Arusha, Tanzania in July 1980.

Having examined the limitations and contradictions of austerity and adjustment programmes unilaterally imposed on African countries, the author lists the criteria which alternatives should fulfil and examines four interrelated issues:

i) the allocation of investment, especially the relative importance of export-oriented, vs. domestic market-oriented activity, agriculture vs. industry, and rural vs. urban development;

ii) the role of the market and the price mechanism in the required resource reallocation vs. that of planning and the public sector;

iii) in the achievement of the desired external balance (however defined) the relative contribution of (a) compression of consumption/imports, (b) export expansion and (c) increased net resource transfers from abroad;

iv) insofar, as reliance is placed on iii) (a) above, 'distribution of sacrifice' between different groups and sectors of the society.

Nature of the Present Crisis

The present crisis is, of course, more than one of severe balance of payments disequilibria aggravated by an acute shortage of external financing. It is also a crisis of growth and development. Since 1981, the majority of the countries on the African continent have been experiencing negative per capita income growth; and the process of economic and social development, for which such high hopes had been held in the decades of the 50s and the 60s, has been at a virtual standstill since the mid-1970s.

Indeed, it is more and more becoming a crisis of survival; of people and of states. More than half of the African countries are now threatened by famine, due to severe shortages of imported foodstuffs in a context where mushrooming urbanization together with lagging domestic food production has given rise to food-dependency. And in more and more countries the viability of the state systems established in the aftermath of decolonization is being undermined, as governments encounter difficulties in meeting monthly payrolls, paying for critically needed oil supplies, or maintaining essential social and public services.

Adjustment Via Austerity

In their single minded pursuit of the necessity of dealing with external imbalance, the austerity programmes that are the subject of this meeting are, if anything, worsening the growth-development crisis in Africa through their heavy reliance on deflationary adjustment which, as has been pointed out, is a disincentive to investment 1/. And we do not even have the consolation of knowing that they restore balance of payments equilibrium. There is compelling evidence that, in the context of current economic conditions, the standard prescriptions of massive public sector retrenchment and devaluations (etc.) have made little, if any contribution to dealing with the balance of payments deficits of the Third World countries. It would be surprising if they were to do so, when the major causes of the present deficits are low commodity prices, stagnating international trade due to the world recession, and the problem of the debt (shortened maturities and high interest rates).

The absurdity of the standard package of measures may be illustrated by posing the following question: how far would a country like Tanzania have to depress its economic activity in order to reduce its consumption of imports to the point where they can be financed by current earnings from exports and capital inflows? Given that most of these imports, such as petroleum, raw materials and food, are non-substitutable by domestic goods, then the logic of this is that a large part of industry and transport would 'need' to close down, and much of the population would 'need' to starve. Adjustment via austerity may well therefore be likened - literally - to an attempt to cure the disease by killing (or perhaps dismembering) the patient.

In international terms, too, the present arrangements for adjust-

ment make very little sense. Repeatedly, it has been pointed out that the Bretton Woods arrangements (whose principal institution, the International Monetary Fund, still remains with us) put all the pressure for adjustment on the deficit countries. No effective provision is made for adjustment of those countries whose payments surpluses are the counterpart of the deficits of others; although as has been cogently argued unilateral adjustment is, by definition, impossible 1/. The paradox is that the country with the largest balance of payments deficits in the world - the United States - is able to escape the strictures of IMF-type austerity programmes. This is as a result of the privileged position of its national currency, which serves as the principal international reserve assets (quite apart from the fact that it is also the dominant force in the International Monetary Fund itself).

'Adjustment, therefore, is a remedy reserved for the weak and the vulnerable: the deficit Third World countries. Even then, those among them which are major exporters of oil and manufactured goods have been able, until recently, to borrow heavily on private international capital markets to finance their current account deficits and sustain their growth. And although they are now staggering under the burden of their own commercial indebtedness, this has given them a form of reverse leverage in the international financial system. The creditor countries are now visibly more worried about the possibility of defaults than the debtor countries themselves. It therefore seems that this select group of Third World countries, principally Latin American, will become the prime beneficiaries of comprehensive debt re-scheduling arrangements. As far as Africa is concerned, the desperate condition of this continent is to be addressed through 'a special action programme of the World Bank' 2/.

If the burden of inter-

national adjustment is thrown on those who are least able to bear it, a similar principle appears to apply to its internal dimensions. Austerity programmes cut real wages through a combination of huge devaluations coupled with money-wage restraint (or freezes), and reduce the 'social wage' by means of cut-backs in the social services and general retrenchment in the public sector while seeking to increase the profitability of business, especially export-oriented business. It is therefore a conscious intention (and not just an accidental by-product) of these programmes, that the major part of the burden of adjustment will take place through compression in the consumption of the mass of the population, while those who are in a position to save and invest should receive enhanced opportunities to do so. The connection between the level of domestic demand and the inducement to invest is, of course, conveniently forgotten, as the model calls for a re-allocation of resources to export activity.

Yet the experience of so many African and Latin American countries shows that these programmes encounter strong resistance from large sections of the population, frequently reflected in the posture of their governments.

The case of the Dominican Republic, where the Government recently suspended negotiations with the IMF after 60 persons had been killed in 'IMF riots' is only one of many 3/. The programmes, aside from being of dubious economic effectiveness, are frequently politically unworkable.

The recent record of the IMF in Africa is quite revealing in this respect. In the period of 1978-1982, twenty-seven African countries concluded a total of forty-nine Stand-by and/or Extended arrangements with the IMF for major loans. Nine of these - nearly 20% of the total - were cancelled prior to their expiration date,

either because the countries no longer considered them necessary or because the IMF was dissatisfied with the country's performance. This does not include cases such as the Tanzanian agreement of 1980, where the arrangement was suspended because the country breached the 'performance criteria' set by the IMF.

Alternative Approaches

A discussion of alternatives to austerity programmes in Africa should therefore fulfill at least three criteria. First, it should address the issue of external balance in the context of long-term growth and development. This includes a discussion of the question, now forgotten, of what is a necessary balance of payments deficit for a country that is actually undergoing a process of development. Secondly, it should deal with both the international and the internal aspects of the adjustment process. And thirdly, it must take into account the political acceptability and work ability of the proposed approach. This is, unavoidably, the most difficult criterion of all, since it involves a great deal of subjective judgement, not to speak of the political self-interest of the various parties.

More specifically, a discussion of alternatives must of necessity deal with at least four issues, recognizing the interrelationships between them:

- i) the allocation of investment, especially the relative importance of export-oriented vs. domestic market-oriented activity, agriculture vs. industry, and rural vs. urban development;
- ii) the role of the market and the price mechanism in the required resource reallocation vs. that of planning and the public sector;

iii) in the achievement of the desired external balance (however defined) the relative contribution of (a) compression of consumption/imports, (b) export expansion and (c) increased net resource transfers from abroad;

iv) insofar as reliance is placed on iii) (a) above, the 'distribution of sacrifice' between different groups and sectors of the society.

Investment/Development Strategy

As far as the first is concerned, it needs to be recognized that the African countries are in a fundamental different position from that of the Third World countries that are exporters of manufactures. The nature of the demand for the primary commodities on which most of them depend is such that wide fluctuations in export prices from year-to-year, coupled with relatively low long-term growth in export volumes (due to low income-elasticities of demand in the main consuming markets) are the norm. Hence, it cannot reasonably be expected that they can 'grow' themselves out of the present crisis through exports. This is not to deny that particular countries may be able to enjoy periods of relatively rapid export expansion based on specific commodities. But as a global strategy for primary commodity exporters, it clearly has severe limitations 4/.

Indeed it seems, to this writer at any rate, that a strong case can be made for a strategy that places rural development and food production at the centre of the stage. Several interesting arguments point in this direction. Firstly, there are the limitations of an export-oriented strategy of growth arising out of the structures of these economies together with the nature of prevailing international economic conditions. Secondly, there is the urgent

pressure of domestic social demand for food arising out of food-import dependency, malnutrition and famine.

A third factor is that the import-intensity of incremental food production is likely to be lower than it is for manufacturing output - although we should also take into account that the mechanization and chemicalization of agriculture will result in growing import demands. A fourth factor is that the urban sector in these economies has been far and away the hardest hit by the present crisis, since it has virtually nothing to fall back on when the supply of imports is drastically curtailed and the prices of such imports rise steeply as a consequence of devaluation and black marketing. The rural sector does have a cushion represented by the possibility of subsistence and semi-subsistence production; although that cushion is undoubtedly neither very large nor very comfortable.

Associated with the strategy of rural development/food production is a policy of industrial development that seeks to promote small and medium-sized industries, both in the rural and urban areas. In the rural areas, such industries may be able to support agricultural development through the simple processing of crop and livestock production. In the towns, they may be able to play a role through the repair and maintenance of the capital stock, and the manufacture of spare parts, in industry and transport. At any rate, an investigation of the potential of such industries may well be worthy of much more attention than is presently the case.

Role of Market Mechanisms

The second issue is the role of market mechanisms vs. government intervention and planning. Here, it is probably necessary to avoid an ideological approach, either of the left or the right. Undoubtedly, many of the 'social-

list' experiments in Africa have foundered on the rocks of inefficient state enterprises and overgrowth bureaucracies. On the other hand, the virtually wholesale dismantling of the public sector and introduction of 'free-market' policies which some powerful international organizations are now crusading for are surely equally misguided. In the market, all actors may be free, but some are evidently more free than others, because they are stronger. Clearly, leaving the market totally open for the powerful transnational corporations and entrenched domestic commercial interests to have their way, could very easily result in distortions in resource allocation that are inconsistent with the broader, long-term development strategy. What seems to be needed here is a more careful evaluation of the costs and the benefits of specific state interventions; an evaluation which takes into account the capabilities as well as the limitations of the governmental apparatus, but which avoids the attitude that such intervention, by its very nature, produces solutions that are inferior to those produced by the 'free market'.

External Balance and Trade Policy

The third issue concerns the determination of the principal macroeconomic variables that are involved in securing external balance: compression of consumption/imports, export expansion and net resource transfers from abroad. It is this which provides the link between the internal and the international aspects of the process. It is in the nature of this issue that the solutions adopted will be dictated by the specific circumstances of individual countries. One has the impression that in many, if not most African countries, imports have already been cut to the bone and even deeper than the bone. In some, there may be further room for compression, but how big a dent will this make on the deficits and what will be the implications for growth and development?

Similarly, there may be some room for export expansion (including tourism) in some countries, and where this is feasible it should certainly be pursued. And in this context, the opportunities for increasing the flow of South-South trade may be more vigorously followed up. Some advantage may be taken of the uneven nature of the development within the South in this connection. Quite a few countries have now achieved a level of industrial development where they have become exporters of technology, and have the capability of engaging in substantial projects of industrial co-operation. Yugoslavia, India, Brazil, the Republic of Korea, and Cuba are examples that spring readily to mind. Frequently, payment for such projects may be made in kind, and they can become the basis for accelerated trade flows. In a similar vein, further opportunities can be pursued for trade and economic co-operation with the socialist countries - whose rate of industrial growth, at least in the last 10 - 15 years, has been considerably above that of the capitalist bloc.

Debt Rescheduling

The case for accelerated net resource transfers from abroad to support 'adjustment-through-growth' is a very strong one, at least on purely theoretical grounds. The problem here is that African countries have very little control over this variable. With a few notable exceptions (e.g. Nigeria, Ivory Coast, Kenya), Official Development Assistance remains the principal source of such transfers for most of these countries and the climate for such ODA is hardly favourable at this time. However, net transfers can be increased not only by argumenting inflows, but also by reducing outflows through, for example, substantial debt rescheduling. Under pressure from the major Latin American debtor countries, the principal creditor countries at the London summit agreed to encourage 'more extend-

ed multiyear rescheduling of commercial debts and standing ready to negotiate similarly in respect of debts to governments and government agencies' 2/.

The question is, will this new round of rescheduling continue to take place, as it has in the past on a bilateral basis? Or, will African countries, and perhaps the Third World as a whole, coordinate their position in this area? The larger Latin American countries have already pointed the way and, in doing so, have opened a path which has made it easier for others to follow.

In May 1984, the presidents of Brazil, Argentina, Mexico and Columbia issued a joint statement in which they warned the North that they cannot accept the 'dangers to democracy and development' represented by existing terms of debt service, specifically the rise in US interest rates 5/. Soon after this, the Dominican Republic suspended negotiations with the IMF on a standby credit facility, Bolivia and Ecuador suspended payment on their foreign debt, and Argentina took the unprecedented step of submitting its own 'adjustment' programme directly to the Board of the IMF, through the Managing Director, rejecting the demands being made by the IMF negotiating team in Buenos Aires 6/. Latin American ministers were to meet in Columbia in June to work out a joint position. Should not African governments do the same and attempt to work out a common front with the Latin Americans? This could be done through one of the existing structures, such as the Group of 77, the Non-aligned Movement, or UNCTAD; it could also be done outside the existing structures entirely.

Conditionality

Central to any programme of expanded IMF and World Bank lending, and any negotiations on debt rescheduling, will be the issue

of conditionality. Of course, the existence of conditionality itself is not in dispute; it is rather the nature of conditionality and the method of its interpretation and application. Third World countries have long argued the need for a big increase in the low-conditionality facilities of the IMF, for example the Compensatory Financing Facility, in cases where their payments deficits are caused by factors mostly outside of their control, such as sudden falls in commodity prices or rises in foreign interest rates. The case for this is, if anything, stronger than ever at the present time. Indeed, the acknowledgement by the London summit of the need to respond to the problems brought upon the Latin American debtor countries by the increases in the US interest rates is another recognition of the validity of this principle.

As regards the Stand-by and Extended facilities of the Fund and Structural Adjustment lending of the World Bank, there is by now overwhelming evidence that the conditionality of the former lays primary emphasis on monetary methods utilized for deflationary adjustment, and that both institutions apply pressure in favour of market-oriented, export led growth. The need here is to press for acceptance of the principle that there is more than 'one road' to external balance; that whereas the need for improvements in economic management and better balance-of-payments performance may be readily conceded, the particular methods and policies that are adopted to bring this about should be considered on their own merits, and not in terms of their consistency with a predetermined adjustment model.

Bretton Woods II

There is a very real possibility that, within the next few years, an international monetary conference will be convened to negotiate a new or at least revised set

of monetary arrangements to replace the Bretton Woods system which broke down in 1971-1973. The necessity for such a conference sometimes referred to as a 'Bretton Woods II' has been envisaged in many quarters for some years 7/. Among the major industrialized countries, the French have been the leading proponent of the idea and the United States has been its chief opponent. However there is growing evidence that the US has accepted that some reform of the present arrangements is inevitable, if only to give some stability to the present exchange rate regime 8/.

It is essential for Africa, and the entire Third World, to have their voice fully heard at such a meeting (at the first Bretton Woods the vast majority of the countries in the Third World were absent being represented by the imperial powers). The amount of technical preparation that will need to go into such a conference, and the events preceding it, is enormous; and these pre-

parations need to start well ahead of time for the position of the Third World to carry real weight.

The Politics of Adjustment

Finally, there is the issue of the 'distribution of sacrifice' among various social sectors in the process. This, above all, is a matter of politics; and in such matters economists are often fools who rush in where those who are much wiser, fear to tread. But it can be noted that a great deal of the resolution of this issue flows out of the solutions chosen for the other issues - for example, the role of the rural sector in the development strategy, the role of the market vs. the state, and the relative degree of compression of consumption vs. net resource transfers from abroad. It is too much to hope that some programmes can be devised through intra-national and international co-operation, which are at least less politically unacceptable than the austerity programmes that are now being proffered?

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